



Mexico: Mexican Steel Sector Overview

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Summary

Steel consumption in Mexico is still considered low compared to consumption in developed nations. While in the United States average annual steel consumption is 350 kilograms per capita, Mexico has an average annual per capita consumption of only 150 kilograms. This illustrates the enormous potential for growth expected in this industry.

Although Mexican steel producers are increasing their production every year, the country still faces several challenges that have hindered Mexico's steel sector development.

Steel imports into Mexico continue to grow and during 2005, 6.8 million tons of steel products were imported from various countries, the United States being the main supplier.

Although Mexico's steel industry has increased its productive base in the last decade, it is still not enough to supply the growing industrial sector. The construction, automotive and home appliance manufacturing sectors are the largest steel consumers in Mexico, and the continuous growth of these sectors will fuel the demand for steel in the country in the following years creating opportunities for U.S. manufacturers of iron and steel products.

State of the Mexican steel industry

Steel consumption in Mexico is still considered low compared to consumption in developed nations. While in the United States average annual steel consumption is 350 kilograms per capita, Mexico has an average annual per capita consumption of only 150 kilograms. This illustrates the enormous potential for growth expected in this industry.

Mexico's steel sector accounts for US\$11 billion, representing ten percent of Mexico's manufacturing GDP. This sector is the largest consumer of natural gas at 26 percent of the country's demand, and the largest consumer of electricity with 7.5 percent of the total consumption in the country. Being an energy intensive industry, steel producers in Mexico suffer from the high costs of energy in the country (high even when compared to rising costs in the United States), which have impacted their profits in the last years.

During 2005, Mexican steel production did not grow at the rate expected, even after 2004 which was considered an exceptionally good year (according to Mexican steel producers there was a boom in the sector). Prices fell in 2005 from January through August due to less dynamic world economic activity, industrial production and steel consumption, resulting in service centers reducing their high inventories. In light of these events, steel producers cut back their production, which set the stage for the 26 percent price increase from August (the time of hurricane Katrina's arrival) to December. This price increase in the last quarter of 2005 was a result of higher scrap prices, recovering industrial production, lower steel import availability and below average inventories after steel service centers had tried to sell as much as possible.

After a very conservative end of year 2005, the steel industry in Mexico expects to continue with conservative growth of 5.5 percent in 2006.

The main Mexican steel consumption markets are the construction sector, automotive production and domestic appliance manufacturing.

The construction sector in Mexico is internally driven and represents nearly half of the total steel consumption in the country. Basic housing construction in Mexico is steel intensive since concrete is the main building material. Steel rebar is the principal product demanded by the Mexican construction industry. The sector is expected to continue steady growth due to an increase in new home financing promoted by the Mexican government through various programs, which have made it easier in the last several years to purchase homes. In 2006, the Mexican National Steel Chamber (CANACERO) expects consumption of rebar to reach three million tons, representing a 7.2 percent increase from last year's demand.

Automotive production is 70 percent export driven and 30 percent domestically driven, representing ten percent of total steel consumption.

Finally, the domestic appliance manufacturing sector is becoming increasingly export driven and currently represents five percent of the total national consumption of steel but continues to grow as well known manufacturers expand their facilities in Mexico. A few leading appliance Original Equipment Manufacturers (OEMs) have had a long term manufacturing presence in Mexico for components, subassemblies and finished appliances. But a recent tide of major investments, starting in the year 2000, is restructuring the appliance sector in the country. The presence of brands such as Whirlpool, GE, Samsung, Maytag, Electrolux and Philips, among others, requires a rising supply of steel for their production processes.

Main steel imports into Mexico

The United States is a constant supplier of steel to Mexico. Of the 0.7 million metric tons of steel mill products exported from the United States on a monthly basis, 20 percent is imported into Mexico, making it the second largest importer of U.S. steel after Canada.

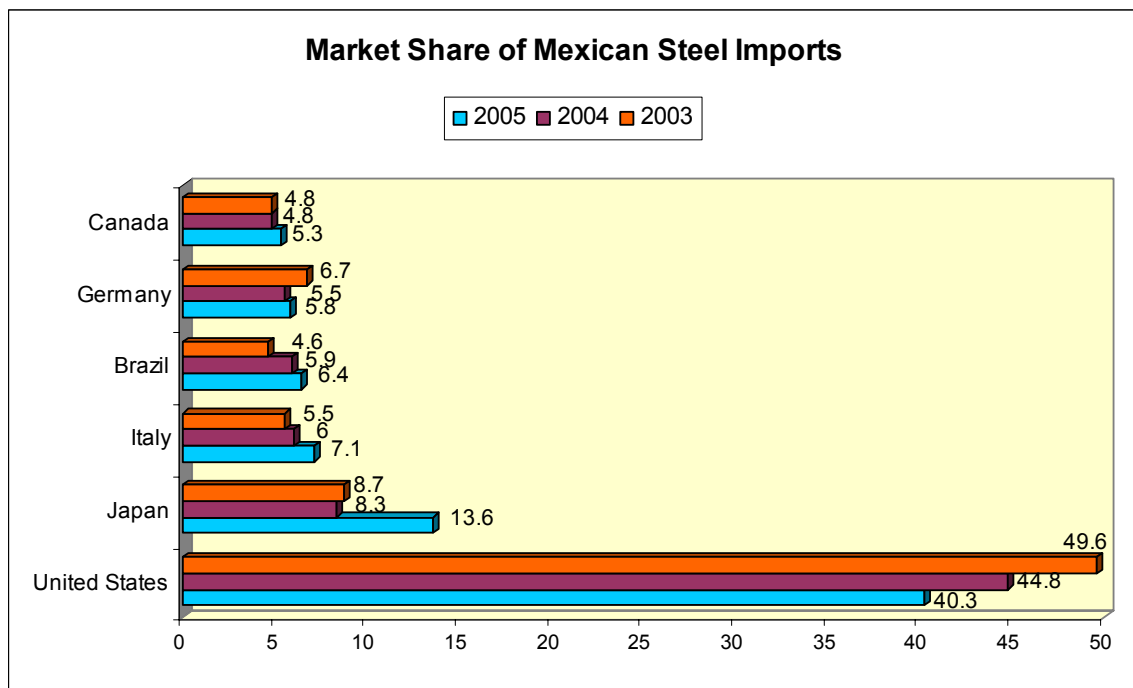
The following table shows the main steel products imported into Mexico during 2005 and the main three suppliers.

HTS code	Main imports into Mexico from the World	1	2	3
7210	Flat rolled iron and nonalloy steel not under 600 mm wide, clad	US	Japan	Germany
7225	Flat rolled alloy steel NESOI not under 600 mm wide	US	Japan	Germany
7208	Flat hot rolled iron and nonalloy steel not under 600mm wide, not clad	US	Japan	Brazil
7219	Flat rolled stainless steel products, not under 600mm wide	Italy	Germany	US
7228	All steel NESOI bars, angles, etc.	Canada	US	South Korea
7204	Ferrous waste and scrap, remelt scrap iron/steel ingot	US	Japan	Germany
7207	Semi finished products of iron of nonalloy steel	Venezuela	US	Australia
7202	Ferroalloys	China	US	South Africa
7209	Flat cold rolled iron and nonalloy steel, not under 600 mm wide, not clad	US	Venezuela	Japan
7216	Angles, shapes and sections of iron and nonalloy steel	US	Spain	Brazil

7211	Flat rolled iron and nonalloy steel under 600 mm wide, not clad	US	Canada	Japan
7214	Bars and rods, hot rolled iron and nonalloy steel NESOI	US	Brazil	Russia
7212	Flat rolled iron and nonalloy steel under 600 mm wide, clad	US	South Korea	Japan
7201	Pig iron, blocks, etc	Brazil	Ukraine	Russia
7224	Alloy steel NESOI in ingots	Brazil	US	Venezuela

Source: World Trade Atlas

Nevertheless, in spite of its geographical proximity to Mexico, the United States has lost nine percentage points of its market share of steel imports into Mexico in the last three years. According to local Mexican steel buyers, this is due to a greater supply of steel products at lower prices that come from South America and Europe. The following chart depicts the percentage of market share of the six main exporters of steel into Mexico.



Source: World Trade Atlas

Forecast

Total Mexican steel production during 2006 is expected to reach 18 million tons. However, CANACERO has predicted that total demand will be 23 million tons during this same year. With demand outpacing domestic supply, Mexico will have to turn to imports to satisfy the domestic demand.

Nevertheless, these forecasts can vary greatly due to the uncertainty brought on by the presidential elections in the summer of 2006 and the strikes in the largest Mexican steel producer, Sicartsa. During the last year of operation, due to strikes the company's production of liquid steel was 500 thousand tons less than planned. This is already having a strong effect on the steel supply in Mexico that will result in

greater demand for steel imports by the end of 2006. The price of rebar in Mexico reached record heights during May 2006 with an increase of 45 percent in the last six months.

CANACERO expects that steel consumption in Mexico will increase at a rate of 3.8 percent in the upcoming year, as the main sectors driving the steel industry in Mexico will continue to grow.

Construction will still represent the largest sector of opportunity for steel producers. Over the last few years, new financing programs for purchasing homes have enabled more and more Mexican workers to own property. As a result, the need for steel products in the construction sector represents an important opportunity for manufacturers of these products. The 16.8 percent increase in the number of new housing credits granted to Mexicans should guarantee solid growth through 2006.

The Mexican steel industry has increased its share of the automotive market and all indications are that the expansion will continue. The automotive OEMs established in Mexico are expected to double their growth rate in the present year.

Consulting firm Harbor Intelligence estimates that the average price of steel products used by the automotive industry in 2005 reached US\$702 per ton. Therefore, sales for 883 thousand tons had a value of US\$1.353 billion. Santiago Clariond, General Director for IMSA, one of Mexico's largest steel processing and galvanizing companies, is forecasting that consumption of flat steel by Mexico's automotive industry will grow to 2,780 thousand tons by 2010, for an average annual growth of 8.1 percent. Metalsa, the main private steel consumer in the auto parts sector in Mexico, is expecting to increase steel consumption by 80 percent in three years, growing from 250 thousand tons in 2004 to 450 thousand tons in 2007. Metalsa Director Jesus Theurel declared recently that the company is going to supply 100 percent of the chassis required by Toyota's new plant in San Antonio, Texas.

Mr. Clariond foresees significant growth in this sector's activity and not only a larger production of complete vehicles, but also investment and migration towards Mexico of auto parts manufacturing plants.

Mexico's major appliance manufacturers will maintain their pace of increase, with an increase of 2.6 percent in their production; OEMs in Mexico will continue to be a driving force demanding steel products.

The Mexican government continues to promote investment in establishing OEM facilities in specific areas of northern Mexico such as Nuevo Leon, Coahuila, Chihuahua, and Baja California. In the upcoming years, there is an expected increase in the number of plants opening in Mexico. One of the sectors that will most likely flourish and requires large supplies of steel is the aerospace industry, with Bombardier establishing in central Mexico, the expansion of the current cluster in the Baja California and Chihuahua area, and the creation of an aerospace cluster in the state of Nuevo Leon.

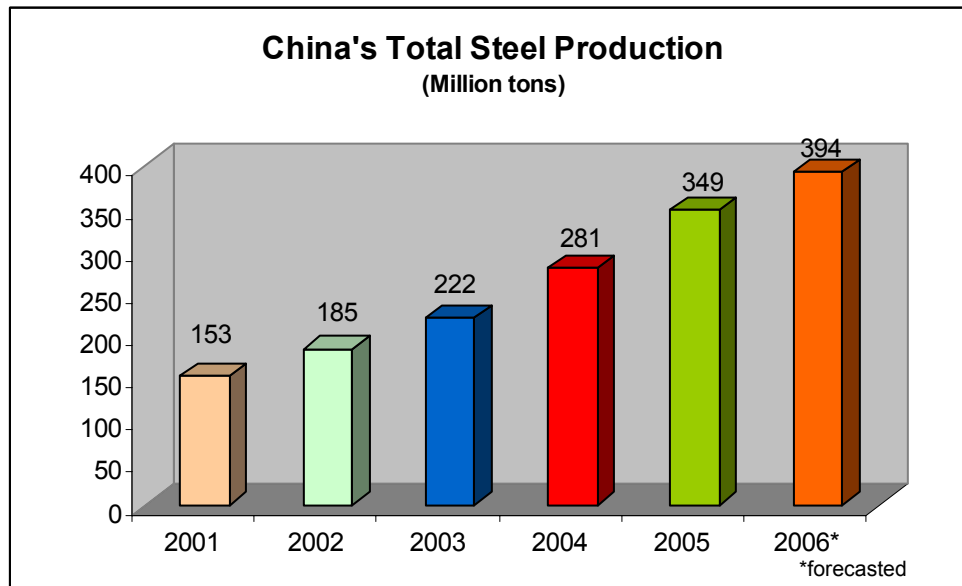
Main challenges for the Mexican steel sector:

Although Mexican steel producers are increasing their production every year, the country still faces several challenges that have hindered Mexico's steel sector development.

China

Not only is China consuming finished steel products and purchasing 50 percent of the world's steel scrap, but by the end of 2006 the country is expected to become one of the world's main steel exporters. With an average growth of 18 percent in the last three years, China's accelerated steel production is having repercussions worldwide creating steel scrap shortage and increasing its price by threefold.

The following chart illustrates the exponential growth in China's steel production in the last five years.



Source: Harbor Intelligence, AMM Presentation in Monterrey, January 2006

High cost of energy

Mexico's manufacturing base is struggling with high energy prices. Over the last four years the cost of natural gas has increased by 217 percent, while electricity costs went up by 70 percent in the same time period. CANACERO and its members continue to pressure the Mexican government to implement structural reforms that would allow the country to have more efficient energy sources. This scenario would enable steel mills and the Mexican industry in general to lower production costs, nevertheless, with the presidential elections coming up reforms seems still far from real. Mexican steel centers increasingly look outwards for suppliers.

Worldwide scrap shortage

There was an increase in the components of steel production in almost a 65 percent in the last 5 years. In 2005 the price of steel scrap increased 57 percent while iron ore prices went up 19 percent in that same period. China has been purchasing scrap to fuel its growing steel sector and it is estimated that now 50 percent of the world scrap supply is purchased by this country. Mexican producers and service centers require suppliers of one of the main resources for steel production.

Need for investment in equipment and machinery

From the beginning of the privatization of the Mexican steel industry in 1991 until 1998, the steel sector in Mexico invested almost two billion dollars in modernizing and updating their industrial facilities. This cost included the purchase of new equipment and facilities to increase steel production.

Mexican steel producers recognize the advantage of modernizing their production base, since the investment that was made during the 90s has put Mexico as the second steel producer in Latin America, after Brazil. Following this trend, Grupo IMSA, one of Mexico's largest steel producer, will invest US\$120 million in the next two years to increase its production base.

Nevertheless, globalization and the purchase of steel mills in the country by foreign companies adds increasing pressure to the need of Mexican steel producers to adopt higher production standards and invest even more in state of the art machinery and consulting services to streamline their processes.

Specifically, steel producers are now looking for ways of making their production process more cost efficient. Equipment that promotes energy savings is in great demand.

Best prospect products in the steel industry in Mexico

Due to the need of construction products and raw material for OEMs operating in Mexico, the demand is high for cold flat rolled steel and structural profiles, rebar, and bars. These products include stainless, alloys and specialty steel, pickled and unpickled hot-rolled sheet, cold-rolled sheet, hot-dipped galvanized steel and electro-galvanized steel among other products.

Ferrous waste and scrap will remain highly demanded by Mexican producers, which are looking for options to source this material in spite of high shipping costs.

Mexico imports steel products from 92 countries around the world but the United States remains the main supplier. During 2006, Mexico is expected to import seven million tons of steel products.

Conclusion

Although Mexico's steel industry has increased its productive base in the last decade, it is still not enough to supply the growing industrial sector. The construction, automotive and home appliance manufacturing sectors are the largest steel consumers in Mexico, and the continuous growth of these sectors will fuel the demand for steel in the country in the following years creating opportunities for U.S. manufacturers of iron and steel products. In addition, the aerospace sector is becoming an important player in Mexican manufacturing, while OEMs continue to establish manufacturing facilities or expand their existing production capacity in the country.

The United States has the strategic advantage of sharing a border with Mexico. As shipping costs continue to soar due to the lack of ships and high fuel prices, this competitive advantage should favor U.S. steel producers that can quickly and inexpensively supply Mexican manufacturers.

How to sell more into Mexico

Mexican steel service centers are increasingly looking for sources of steel scrap and products. Local Mexican steel service centers can act as representatives or distributors for U.S. steel mills. Nevertheless, contacting local Mexican companies can also provide new clients. The Commercial Service provides numerous services to help you locate business partners in Mexico.

U.S. suppliers should take advantage of Mexico's proximity and think about using railroad as an advantageous shipping means. For example, for US\$2,100 railroad can carry 80 tons of steel products from Houston, Texas to Monterrey, Mexico, while a truckload carries only 20 tons at a cost of US\$950.

Preferred shipping terms are FOB in a city close to the U.S. border with Mexico where the Mexican importer will arrange the transportation and paperwork to bring the product into the country. When negotiating with a Mexican company, the U.S. exporter should be clear on the terms of the transaction to make sure no misunderstandings arise from this. On personal interviews with local Mexican service centers, one of the main problems they expressed having with U.S. suppliers was the different interpretation of International Commercial Terms (INCOTERMS).

Sources for market intelligence

Mexican Steel Chamber - CANACERO
<http://www.canacero.org.mx>

This site includes a list of associates of this organization as well as direct links to their respective websites. Additional information includes a list of standards and statistical reports on national production, trade balance, imports, exports and outlooks on the Mexican steel industry.

Latin-American Institute for Iron and Steel - ILAFA

<http://www.ilafa.org>

ILAFA is an organization created in 1959 by steel producers in Latin America. The website includes a directory of members by country that include producers of iron and steel products.

Ask Harbor

<http://www.askharbor.com>

Consulting firm specialized in market analysis.

For More Information

The U.S. Commercial Service in Monterrey, Mexico can be contacted via e-mail at:

yazmin.rojas@mail.doc.gov; Phone: 011-52-81-8343-4450 Fax: 011-52-81-8342-5172 or visit our website: www.buyusa.gov/mexico/en.

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